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H PLEASE PASS TO CONGRESSMAN MARKEY

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SUBJECT: SCENESETTER FOR CODEL MARKEY

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¶1. (SBU) Summary: Brazil's democratic institutions are generally strong and stable, and President Luiz Inacio Lula da Silva remains popular because of his orthodox economic policies and expanded social programs. Export-led economic growth has been the norm in the recent past, while Brazil has supported reasoned foreign policy goals and has steadfastly supported democracy in the hemisphere. In the bilateral relationship, the U.S. and Brazil share many basic goals, although Lula seeks to balance good relations with the developed world with South-South foreign policy initiatives. Brazil's ethanol program has made it a global model for alternative energy and offers potential for bilateral cooperation on an important strategic issue. On the environment, Brazil has long been on the defensive about the ongoing, extensive deforestation of the Amazon, which has made Brazil one of the leading producers of greenhouse gases.

End summary.

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Latin America's Democratic and Economic Powerhouse
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¶2. (SBU) Brazil's democratic institutions are generally strong and stable, and the military dictatorship that ended over 20 years ago is consigned to the dustbin of history, as Brazil's armed forces today pursue a professional non-political identity. A year following his re-election to a second term, and despite prosecution of high-level members of his administration on corruption charges, President Luiz Inacio Lula da Silva remains a personally popular president as a result of his orthodox economic policies and expanded social programs. Ongoing and public scandals involving the leadership of the Senate and various members of congress have led to low ratings for the institution among the Brazilian public. Increasingly, the court system has taken steps to curb impunity among public officials, which have been well received by a public accustomed to abuses by authorities.

¶3. (SBU) On the economic front, Lula's Finance Minister Mantega, Planning Minister Bernardo, and Central Bank President Meirelles have maintained broadly orthodox policies. In January, Lula unveiled his Growth Acceleration Program (PAC), consisting of public investment promises and targeted tax breaks aimed primarily at construction and certain high tech sectors, which has become the economic policy centerpiece of his second administration. Although the PAC contains many measures of incremental merit, it does not address some of the growth-limiting distortions in the economy, burdensome tax and fiscal structure and onerous labor and business regulations. Lula's social programs, combined with formal sector job growth and real increases in

the minimum wage, have reduced income inequalities each year since 2004. Higher economic growth will be required, however, to lift the masses out of poverty.

¶4. (SBU) With steady export-led economic growth having become the norm in the recent past, Brazil has been a supporter of reasoned foreign policy goals and has been steadfast in its support of democracy in the hemisphere. The attainment of a permanent seat on the UN Security Council has been a central tenet of Brazil's foreign policy under President Lula da Silva's government. More generally, Brazil seeks to play a leadership role on the global stage by, among other things, playing a central role in the G-20 at the WTO, and leading the UN peacekeeping force in Haiti, which could serve as a springboard to greater international leadership on democracy promotion and security issues. Brazil's efforts to build South-South relations continue to dominate its foreign policy, sometimes to the detriment of core political and economic interests. The GoB, along with India, has led the G-20, a group of developing nations coordinating negotiating positions for the WTO Doha Round. The group's widely varying membership has made it difficult for them to reach consensus on negotiating positions. Brazil has not yet signed an IAEA Additional Protocol, although it has not ruled out signing it in the near future. Most recently, Brazil has announced its desire to join OPEC following the discovery of massive offshore reserves of oil and gas.

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The Bilateral Relationship
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¶5. (SBU) The U.S. and Brazil share the basic goals of fostering hemispheric stability, promoting democracy,

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achieving a mutually satisfactory conclusion to the Doha round of WTO negotiations, preventing terrorist and drug transit activity, and supporting international non-proliferation regimes. U.S.-Brazil cooperation is often limited by the GoB's unwillingness to take action regarding threats to democracy in specific countries and to support aggressive action in multilateral forums on such issues as non-proliferation, human rights, and democracy.

¶6. (SBU) Although under President Lula Brazil has stressed South-South relations, Brazil's status as a leader in biofuels, combined with the March 2007 signing our bilateral MOU on biofuels cooperation, offers a potential avenue for increasing bilateral cooperation in a strategically important area. The two presidential summits in March 2007 (Sao Paulo and Camp David) have helped create a positive tone in our bilateral conversation.

¶7. (SBU) Our bilateral dialogue with the GoB on development assistance to Brazil and in third countries contains positive elements, including promising potential in biofuels. It is constrained by differences in approach to anti-poverty efforts, with the GoB focusing on cash transfers, while the USG prefers more finely targeted assistance. The Brazilian Government's multi-billion dollar poverty alleviation program -- Bolsa Familia (Family Stipend) -- receives technical assistance from the World Bank and IDB. USG budget constraints and the fact that it is a cash transfer program (albeit with conditions) keep the USG from actively cooperating with the initiative. USAID has sought to target its USD 8 million in programs for Brazil towards promoting sustainable livelihoods through working on issues such as health, the environment, and small and medium-sized enterprises.

¶8. (SBU) The GoB has a strong interest in hemispheric security issues, and cooperates with the USG on the operational level in the fight against terrorism and drug trafficking. Brazil has been cautious about taking an active role in recent high-profile non-proliferation efforts.

Brazil remains an active partner in the DHS's Container Security Initiative (CSI) and has expressed approval of the Proliferation Security Initiative (PSI). However, the GoB has not yet endorsed the PSI statement of principles.

Biofuels -- Potential for Strategic Cooperation

¶9. (U) Brazil has transformed a 1970s program to bolster its large sugar-cane sector into a remarkable showcase for biofuels. The success of Brazil's ethanol program has made it a model for the world in terms of alternative energy and presents the potential for bilateral cooperation on an important strategic issue. Brazil's comparative advantage is its ability to produce huge quantities of sugarcane, which is currently the most efficient feedstock for ethanol. Cane requires far less processing than corn to produce ethanol. According to the World Bank, at current prices, Brazil can make ethanol for about one US dollar per gallon, compared with the international price of about USD 1.50 per gallon for gasoline. On the demand side, Brazil's use of modest tax breaks have led new car purchasers to opt overwhelmingly for "flex-fuel" cars that can run on either gasoline, ethanol, or any combination of the two.

¶10. (SBU) Following the signing of the MOU in March, Brazil and the United States have been seeking ways to increase our collaboration in order to develop the next generation of biofuels, as well as in developing international standards on biofuels which should facilitate greater international acceptance and use of biofuels.

Agriculture Trade Disputes

¶11. (U) Brazil, like Canada, made a first request to establish a WTO Dispute Settlement panel on November 19, 2007, to challenge US agricultural domestic support, claiming the US exceeded support caps 1999-2002 plus 2004-2005. A second panel request and the establishment of the panel are expected on December 18. In 2004, the WTO found mainly in Brazil's favor in the challenge against US cotton programs. Brazil challenged US compliance with the Panel report and the Panel found again primarily in Brazil's favor in October 2007 (although the report remains WTO-confidential until formally released in December). Some in the Brazilian congress threatened cross-retaliation against IPR in the cotton case,

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but to date legislative proposals have not moved forward. News reports have indicated that the Foreign Ministry is preparing such cross-retaliation measures should the WTO find in their favor.

Deforestation and Climate Change

¶12. (SBU) On the environment, Brazil has long been on the defensive about the ongoing, extensive deforestation of the Amazon, which has made Brazil one of the leading producers of greenhouse gases. Over the last three years, the rate of deforestation has dropped sharply. Brazil now views the debate over climate change as an opportunity. It proposes that the international community provide financial incentives for avoiding deforestation and vigorously promotes the use of biofuels. In the last five months of 2007, however, the rate of deforestation has risen dramatically. The Environment Minister and independent experts attribute the increase in deforestation largely to the substantial increase in agriculture commodity prices.

¶12. (SBU) Brazil pursues two sometimes conflicting goals with regard to the Amazon region. On the one hand, it seeks

to preserve much of the natural resources and biodiversity found in the region. The Forest Code requires the landowner to maintain 80 percent of the forests on the land. Further, the GoB has placed large amounts of the forest into protected areas, such as national parks and indigenous reserves. At the same time, the GoB seeks economic growth and redistribution of land. Thus, since the 1970s it has built a network of roads through the Amazon, which has opened the region to timber and agriculture (mainly soybean) interests. The GoB has resettled many of the poor into settlements along the roads, and as a result, in 2004 the deforestation rate shot up to a high of 27 thousand square kilometers per year. High demand for charcoal to support a rapidly growing pig iron industry has also contributed to significant deforestation. Nonetheless, a combination of market forces and government actions has led to an almost 50 percent reduction in the deforestation rate.

¶13. (SBU) The GoB created a Forest Service in 2006 and is seeking to obtain a stronger grip on forest management. It also has ratcheted up somewhat the enforcement of existing rules against deforestation. These measures are aimed at avoiding a return to the very high deforestation rates earlier in the decade.

¶14. (SBU) With respect to climate change, the GoB has proposed that the international community providing financial incentives for avoiding deforestation. In addition, it uses the focus on renewable energy to promote greater use of biofuels. The GoB, however, is adamantly opposed) as a developing country - to accepting international, binding obligations that would impede economic growth, such as restrictions on the use of its natural resources. Brazil is sensitive about any suggestions on how it should manage the Amazon.

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